Supreme Court, U.S.
FILED
JAN 19 1994
OFFICE OF THE CLERK

Nos. 92-1384 and 92-1839

In The
Supreme Court of the United States
October Term, 1993

BARCLAYS BANK PLC,
Petitioner,
vs.
FRANCHISE TAX BOARD,
An Agency of the State of California,
Respondent.

COLGATE-PALMOLIVE COMPANY,
Petitioner,
vs.
FRANCHISE TAX BOARD,
An Agency of the State of California,
Respondent.

On Writs of Certiorari to the Court of Appeal of the State of California in and for the Third Appellate District

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BRIEF OF AMICI CURIAE IN SUPPORT OF RESPONDENT FRANCHISE TAX BOARD BY SENATORS BYRON L. DORGAN, TED STEVENS, FRANK H. MURKOWSKI, JUDD GREGG, AND ROBERT C. SMITH

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QUESTION PRESENTED

When the United States Senate has carefully studied and unambiguously rejected a treaty provision that would bar the States from employing a particular method of corporate tax accounting for foreign corporations, should the Judiciary nevertheless prevent a State from using this method of accounting under the dormant authority of the Foreign Commerce Clause?

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INTEREST OF AMICI

Amici are members of the United States Senate. This case presents this Court with issues involving the proper roles of

the Executive Branch and the Senate in establishing United States policy through the treaty mechanism. Amici, as members of the United States Senate, have a unique and vital interest in these questions and, in particular, the significance to be attached to the actions of the United States Senate in declining to give its advice and consent to a treaty presented to it by the Executive Branch, as required for ratification by the Constitution of the United States.

STATEMENT PURSUANT TO RULE 37

This brief is submitted pursuant to Rule 37.3 of this Court in support of Respondent Franchise Tax Board, State of California. The consent of counsel to the filing of this brief has been obtained and has been or will be filed with the Clerk of this Court in due course.

SUMMARY OF ARGUMENT

The United States Senate was asked to give its advice and consent to a tax treaty between the United States and the United Kingdom which would have prohibited the States from using the unitary method of tax accounting with respect to multinational businesses domiciled in the United Kingdom. After intensive consideration, the Senate refused to give its advice and consent to the Treaty with this prohibition. This refusal was made in fulfillment of the Senate's constitutional role as a protector of State sovereignty. With all due respect and deference to the wisdom which this Court possesses and exhibits, it is respectfully submitted that this Court should not intervene in this matter so as to overrule the judgment made by members of the Senate.

ARGUMENT

THE SENATE'S REFUSAL TO CONSENT TO A TREATY IS AN ACT OF CONSTITUTIONAL SIGNIFICANCE

The cause here is the right of States of the United States to choose the mode of tax accounting to be used in the raising of state revenue. At issue also is the constitutional integrity of the United States Senate.

The unitary method of tax accounting is an integrated, conceptually fair basis of taxation which seeks to negate the intense complexities of intercorporate international tax accounting embodied in the "arm's-length" method. The arm's-length method treats each legal corporate entity as if it were real, while ignoring the identity of the whole enterprise. The unitary method identifies the income of the whole and then apportions that income according to the proportionate contribution of the taxing State.

The constitutional integrity of the United States Senate is at stake because of the risk that the Supreme Court of the United States will ignore the Senate's constitutionally given power to play a role in the balance to be cast between state and local power on the one hand and foreign policy on the other.[1] The Constitution empowers the Senate, as part of the

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[1] In prior decisions, this Court has exhibited its sensitivity to the Senate's role in our federal structure. For example, in *Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528 (1985) at 551-552, this Court stated:

> The extent to which the structure of the Federal Government itself was relied on to insulate the interests of the States is evident in the

(continued...)

Congress, to regulate commerce, interstate and foreign, and to advise and consent in the making of treaties of agreement with foreign nations.

In the circumstances of the present case, the Executive Branch sought the advice and consent of the Senate to a treaty negotiated with Great Britain about terms of trade. High in priority among the provisions sought by Great Britain was agreement by the United States to impose a ban upon States from using unitary methods of tax accounting. The treaty would have imposed the "arm's-length" method on all of the States of the United States by the constitutional supremacy of treaties over domestic law.[2] Great Britain, in these

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[1](...continued)
views of the Framers. James Madison explained that the Federal Government "will partake sufficiently of the spirit [of the States], to be disinclined to invade the rights of the individual States, or the prerogatives of their governments." [citation omitted] . . . "it was a favorite object in the Convention" to provide for the security of the States against federal encroachment and that the structure of the Federal Government itself served that end. [citation omitted] . . . equal representation of the States in the Senate, which he saw as "at once a constitutional recognition of the portion of sovereignty remaining in the individual States, and an instrument for preserving that residuary sovereignty." [citation omitted] . . . "the residuary sovereignty of the States [is] implied *and secured* by that principle of representation in one branch of the [federal] legislature" (emphasis added). [citations omitted] . . . the Framers chose to rely on a federal system in which special restraints on federal power over the States inhered principally in the workings of the National Government itself, rather than in discrete limitations on the objects of federal authority. State sovereign interests, then, are more properly protected by procedural safeguards inherent in the structure of the federal system than by judicially created limitations on federal power.

[2] U.S. Const., art. VI, § 2.

negotiations, may be seen as speaking for the international multinational corporate and banking interests that want to take advantage of United States markets and natural resources without having to account for any of the benefits which flow between local activities and the rest of their global enterprises.

The Senate intensely considered the request of the Executive Branch for its advice and consent to this treaty.[3] The Senate responded, rejecting the treaty as written, consenting to its ratification only without the ban on the use by the States of the unitary method of accounting.[4] The Senate continued to attend to the issue intensively until the problem was significantly resolved through political channels in the mid-1980's.[5]

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[3] 124 Cong. Rec. 18402-18430, 18651-18670 (1978).

[4] 124 Cong. Rec. 18670, 18709-18712 and 19076-19078 (1978).

[5] Various committees of the United States Congress have held hearings on the issues of state taxation including the use by the states of unitary reporting. The hearings listed below indicate the intensity, both in depth and time of consideration:

> Report of the Subcommittee on State Taxation of Interstate Commerce of Committee on Finance on S. 1245 (Mathias) and S. 2092 (Magnuson) (490 pages); Committee on Ways and Means, 95th Congress, 1st Sess., Recommendations of the Task Force on Foreign Source Income (Comm. Print 1977); Senate Committee on Foreign Relations, Third Protocol to the 1975 Income Tax Convention with the United Kingdom of Great Britain and Northern Ireland as Amended, S. Doc. No. 5, 96th Cong., 1st Sess. (1979) (150 pages); Tax Treaties with the United Kingdom, the Republic of Korea, and the Republic of the Philippines, 1977: Hearings Before the Senate Committee on Foreign Relations, 96th Cong., 1st Sess. (1977) (496 pages); State Taxation of Interstate Commerce and Worldwide Corporate Income, 1980: Hearings on S. 983 and S. 1688 Before the Subcomm. on Taxation and Debt Management Generally of the Senate
> (continued...)

Now the multinational corporate interests try a different tack, here direct to the United States Supreme Court for a ruling from the Justices that unitary approaches to taxation should be banned under the authority of the Foreign Commerce Clause where multinational corporations are concerned. The premise of Petitioners' claim is that Congress has not spoken on the issue of a ban on States wishing to use other than arm's-length accounting, that the Federal Government must speak on this issue with "one voice," and therefore the Judiciary should dictate the arm's-length method under the dormant authority of the Foreign Commerce Clause. But to say, in this situation, either that the Congress has not expressed itself or that the situation requires one and only one approach, blinks reality.[6] Because the Senate has spoken in its constitutional voice,[7] the California tax is permissible.

To grant the petitioners' request would constitute an institutional insult to the Senate. The Executive Branch invoked Senatorial process, and does not assert the inconsequence of resulting Senatorial action. Since the Senate's rejection of the ban, the Executive has repeatedly

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[5](...continued)
Comm. on Finance, 96th Cong., 2d Sess. (1980) (982 pages); Unitary Taxation, 1984: Hearings Before the Subcomm. on International Economic Policy of the Senate Foreign Relations Comm., 98th Cong., 2d Sess. (1984) (445 pages); Interstate Taxation, S. 2173: Hearings Before the Senate Committee on the Judiciary, 95th Cong., 1st and 2d Sess. (1977-1978) (957 pages).

[6] *Wardair Canada v. Florida Dept. of Revenue*, 477 U.S. 1, 11-12 (1986), establishes that rejection of treaty provisions can have legal significance for Foreign Commerce Clause analysis.

[7] U.S. Const., art. II, § 2, cl. 2.

recognized the Senate's position and has made no effort to circumvent it. Instead, conflicts over tax accounting methods have been further negotiated through diplomatic and political processes.[8] California changed its law substantially in 1986,[9]

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[8] The Executive Branch negotiated the United States/United Kingdom Tax Convention with the United Kingdom in 1975. In transmitting the proposed treaty to the Senate for its advice and consent, the Executive Branch noted, "A second new provision is found in paragraph 4 of Article 9 (Associated Enterprises). This provision represents the *first attempt* to bind State and local taxing authorities by a substantive provision of the treaty (other than non-discrimination)." (Emphasis added). Letter of Submittal, June 8, 1976, 3 Tax Treaties Reporter (CCH) ¶ 10,938. The Executive Branch then negotiated the Third Protocol to the Treaty to reflect the action of the Senate. In a summary of the Protocol prepared for the Senate Foreign Relations Committee, the first modification is described by the Executive Branch as follows:

> "In conformity with the Church reservation, the protocol makes Article 9(4) of the proposed treaty, which restricts the use of the worldwide combination/unitary method of apportioning income, inapplicable to state or local governments. The provisions of Article 9(4) would continue to apply, however, to the United States and United Kingdom governments." Third Protocol to the 1975 Income Tax Convention with the United Kingdom of Great Britain and Northern Ireland, as Amended: Report of the Committee on Foreign Relations, United States Senate; S. Doc No. 5, 96th Congress, 1st Sess. (1979)

In 1979 in response to a question by Senator Church, Assistant Secretary of Treasury for Tax Policy, Donald C. Lubick, submitted the following explanation to the Committee on Foreign Relations of the United States Senate as to why state taxes were not included by the administration in its own Model Income Tax Treaty:

> "These local U.S. taxes are not covered because it is unlikely that the United States would consent to the ratification of any treaty provision that restricted the rights of the various states to impose their own taxes." *International Tax Treaties: Hearing before the Senate Comm. on Foreign Relations*, 96th Cong., 1st Sess. (June 6, 1979), p. 112 (statement of Donald C. Lubick).

(continued...)

with refinements in 1993,[10] which led the Executive Branch, through the Solicitor General, to suggest to this Court the wisdom of declining to hear the present case and refraining

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[8](...continued)

During consideration of the proposed Unitary Tax Repealer Act in 1985, Roger Mentz, Assistant Secretary of the Treasury for Tax Policy, testified for the Executive Branch as follows:

> "I am pleased to report that, since the introduction of the legislation, Idaho, New Hampshire, Utah, and, on September 5, California, have enacted "water's edge" legislation. The Administration applauds these states' actions. These state legislative developments go a long way toward resolving the difficult unitary tax issue. Moreover, they illustrate the *successful* operation of the Federal system. . . . We have not . . . reached the end of the road with respect to this issue. . . . *We believe, however, that such significant progress has been made that restrictive Federal legislation is not warranted at this time.*" *Review of Unitary Method of Taxation: Hearing Before the Subcommittee of Finance on Taxation and Debt Management of the Committee on Finance on S. 1113 and S. 1974*, 99th Cong., 2d Sess. (September 29, 1986), p. 71. (Emphasis added).

In transmitting the 1973 Income Tax Convention with the Union of Soviet Socialist Republics to the Senate Foreign Relations Committee, the State Department made the following statement regarding "Taxes Covered" in the Technical Explanation: "The taxes imposed by the Union Republics of the Soviet Union (comparable to states of the United States) are not covered by the Convention because, *in keeping with past U.S. policy the taxes of the state and local governments of the United States* are excluded from the scope of the Convention, except for purposes of Article X (Nondiscrimination)." (Emphasis added). 3 Tax Treaties Reporter (CCH) ¶ 10,630 p. 44,029.

[9] Ch. 660, Cal. Stats. 1986.

[10] Ch. 881, Cal. Stats. 1991.

from taking a position in support of Petitioners on the merits.[11]

We in the Senate do not understand the Supreme Court of the United States to have been anything but sensitive in the past to the balance and separation of powers among the Federal branches and the States in respect to judicial interpretation of the Foreign Commerce Clause. The Supreme Court's opinion in *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. 159 (1983), sets the framework with a remarkably direct and able dissection of the foreign commerce problem, holding that California had no obligation under the Foreign Commerce Clause to employ the "arm's-length" method, as long as application of its unitary approach is fair.

Yet it is incumbent upon us, not as supplicants only before a great court, but as friends of the court asserting equal stature for the institution of the Senate and equal strength in the balance of the power of our Nation, to say that the Federal Government does not speak, need not speak, and should not be made to speak with the "one voice" to impose the "arm's-length" method of taxation upon the separate States.

We assert the constitutional entitlement of the United States Senate to a role of principal in the making of international treaty arrangements. We ask the Supreme Court

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[11] Brief of United States, October 7, 1993, *Barclays Bank PLC v. Franchise Tax Board*, p. 10-11.

of the United States not to allow our role and process to be ignored and overridden.

Dated: January 19, 1994

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